Eidgenössische Finanzmarktaufsicht FINMA
Autorité fédérale de surveillance des marchés financiers FINMA
Autorità federale di vigilanza sui mercati finanziari FINMA
Swiss Financial Market Supervisory Authority FINMA

Occupational pension schemes of life insurance companies

Group life reporting 2018: transparency report

Key points

Foreword

The abridged English version of this report contains the key points. The full version of the report is available in German and French at https://www.finma.ch/en/documentation/finma-publications/reports/transparency-report-second-pillar/.

Key points

Occupational pension schemes: the role of private life insurers
Occupational pension schemes are managed and safeguarded by occupational pension institutions, which are legally autonomous and subject to the Federal Act on Occupational Retirement, Survivors' and Disability Pension Plans (OPA).

Private life insurers which take on the risks and capital management responsibilities of occupational pension institutions in full or in part (group life insurers) are subject to the Insurance Supervision Act (ISA). They assume part or all of the risk coverage and capital management from occupational pension institutions by reinsuring and providing full or partial coverage of the risks which the latter cannot or do not want to assume. These group life insurers manage approximately one-fifth of all pension assets totalling CHF 1,104 billion, insure risks of almost half of the 4.18 million active insured persons (including those with only risk cover), serve around one-fifth of the 1.14 million pensioners and satisfy most of the demand of SMEs for full coverage insurance solutions.[1]

Group life insurers operate in a strictly regulated area of social insurance. In this context, FINMA is mandated to ensure that the assets entrusted to them for occupational pensions are secure. Guaranteed insurance obligations are comprehensively covered by separate tied assets which are subject to strict investment requirements with respect to quality, risk diversification, permitted asset classes, risk management and administration.

Group life reporting and minimum ratio
The group life report prepared by life insurers active in the occupational pensions sector focuses solely on this part of their business.

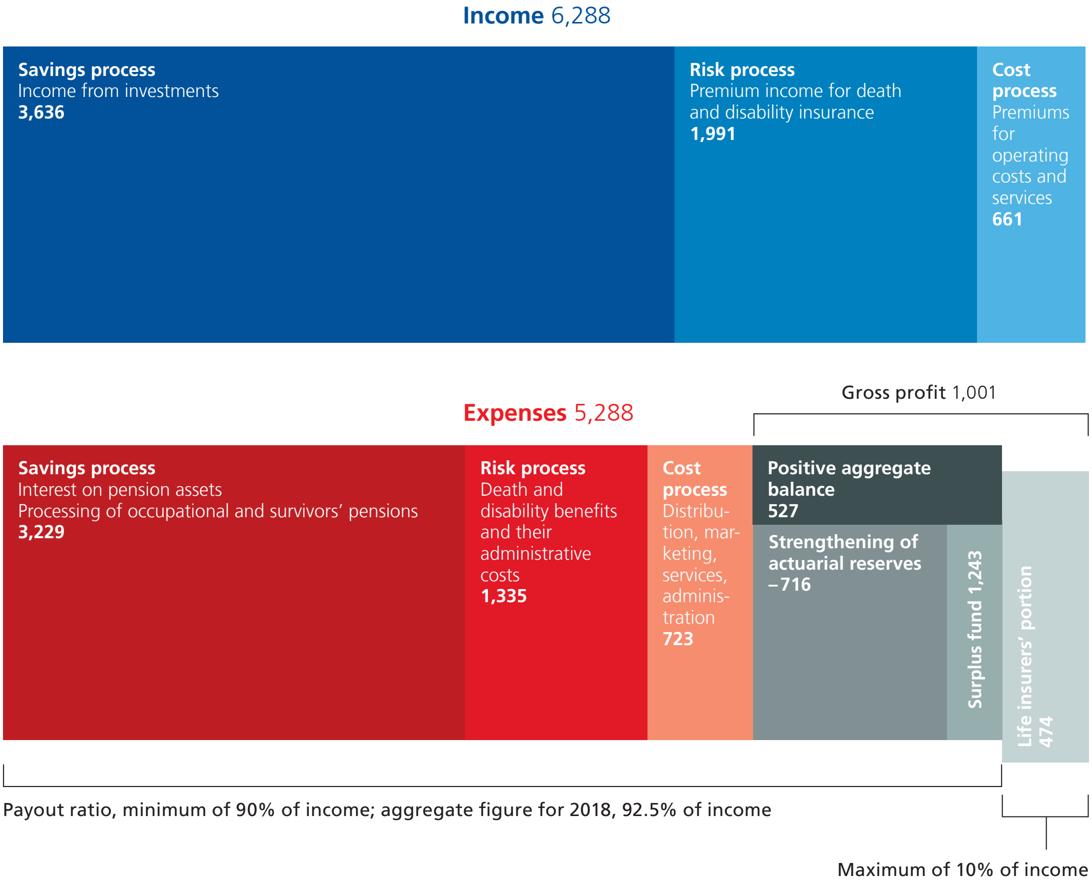
The operating statement comprises the balance sheet items and income statement items and includes statistics and other information, as well as a technical segregation whereby income, expenses and gross result are split across the savings process, the risk process and the cost process. This increases the transparency of income and expenses in occupational pensions, particularly regarding compliance with the rules on calculating and distributing the surplus.

The income and expenses for the three processes are set out in Figure 1. The gross result is divided into the positive overall balance (which is allocated to the insured occupational pension institutions and their insured persons) and the group life insurers' share. The minimum ratio is the share which must be allocated by law to the community of insured persons. The Federal Council has ruled that 90% of income – i.e. at least 90% of premium income (excluding savings premiums) and investment income – must normally be allocated to the community of insured persons (Art. 147 ISO). Savings premiums are credited in their entirety to the insured persons.

[1] Allianz Life, Baloise Life, Helvetia Life Insurance, PAX, and Swiss Life still offer full coverage insurance (as at 2018).

Distribution of the gross result from group life business: at least 90% of the income goes to the community of insured persons and at most 10% to the life insurers (Figure 1)

Figures for business subject to the minimum ratio from the 2018 group life reporting (in CHF millions)



Income, expenses and result, 2014–2018 (Figure 2)

In CHF millions	2018	2017	2016	2015	2014
Savings process					
Income	3,954	3,816	4,767	5,186	5,351
Expenses	3,459	3,146	3,271	3,329	3,354
Result	495	670	1,496	1,857	1,997
Risk process					
Income	2,479	2,463	2,528	2,594	2,624
Expenses	1,635	1,454	1,452	1,418	1,395
Result	844	1,009	1,076	1,176	1,229
Cost process					
Income	747	754	754	757	744
Expenses	786	773	757	797	824
Result	–39	–19	–3	–40	–80
Summary of the three results					
Savings process result	495	670	1,496	1,857	1,997
Risk process result	844	1,009	1,076	1,176	1,229
Cost process result	–39	–19	–3	–40	–80
Gross result (group life reporting)	1,300	1,659	2,569	2,994	3,146
Strengthening technical reserves[2]	776	–612	–1,592	–1,847	–1,651
Net result	2,076	1,047	977	1,147	1,494
Breakdown of the net result					
Assignment to surplus fund	1,542	493	375	509	808
Operating result[3]	534	554	602	638	686
Net result	2,076	1,047	977	1,147	1,494

[2] Release from strengthening technical reserves minus strengthening of actuarial reserves.
[3] The operating result corresponds to the life insurer's share of the net result.

Income, expenses and result for 2018: stable operating result thanks to release of provisions no longer required

2018 is the fourteenth consecutive year in which private life insurers have accounted for their occupational pension scheme activities in their group life reporting. The key focus of business during the past year was on financial stability and on ensuring that insurers can meet their commitments in the long term in view of the prevailing very low interest rates.

Following the difficulties encountered in 2008, they reported an overall positive result for the tenth consecutive time. Figure 2 shows the results of the savings process, risk process and cost process. They give an aggregate gross result of CHF 1,300 million

(CHF 1,001 million of which is for business subject to the minimum ratio), representing a year-on-year fall of CHF 359 million. This is primarily due to poorer results from both the savings and the risk processes.

Life insurers were able to release technical provisions no longer required amounting to CHF 776 million (the previous year saw strengthening by CHF 612 million). This gives a net result of CHF 2,076 million, of which CHF 1,542 million goes to the surplus fund, leaving an operating result of CHF 534 million. This means that the operating result declined once again, despite a further increase in total assets.

The provisions no longer required and consequently released during the reporting year also benefited insured persons with around CHF 1 billion more going to the surplus fund than in the previous year, in total CHF 1,542 million (2018: CHF 493 million). It is significant that the results from the risk process are clearly lower as a result of higher expenses, while risk premiums remained stable.

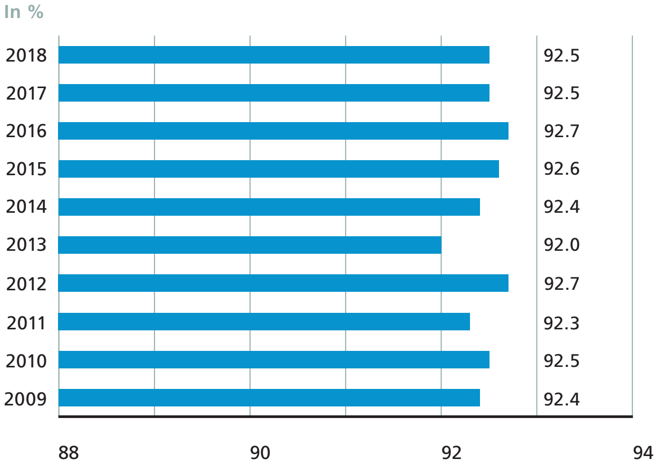
Payout ratio for 2018

For group insurance contracts with a statutory minimum ratio, the aggregated payout ratio for 2018 was 92.5%, remaining stable and above the statutory minimum of 90%.

Almost two thirds of the substantial increase in the surplus fund of CHF 1,542 million can be attributed to AXA, which was able to release provisions no longer required to the surplus fund in the course of its transformation from a full coverage insurance provider to a risk insurer. Another reason was the fact that the release of provisions for the inflation of risk-pensions subject to the OPA no longer required led to fewer reserve reinforcements having been necessary than in the previous year at many companies, meaning that more money could be allocated to the surplus fund.

Life insurers active in the occupational pension scheme sector reported an aggregate annual pre-tax result of CHF 534 million for 2018 (2017: CHF 554

Payout ratios since 2009 (Figure 3)



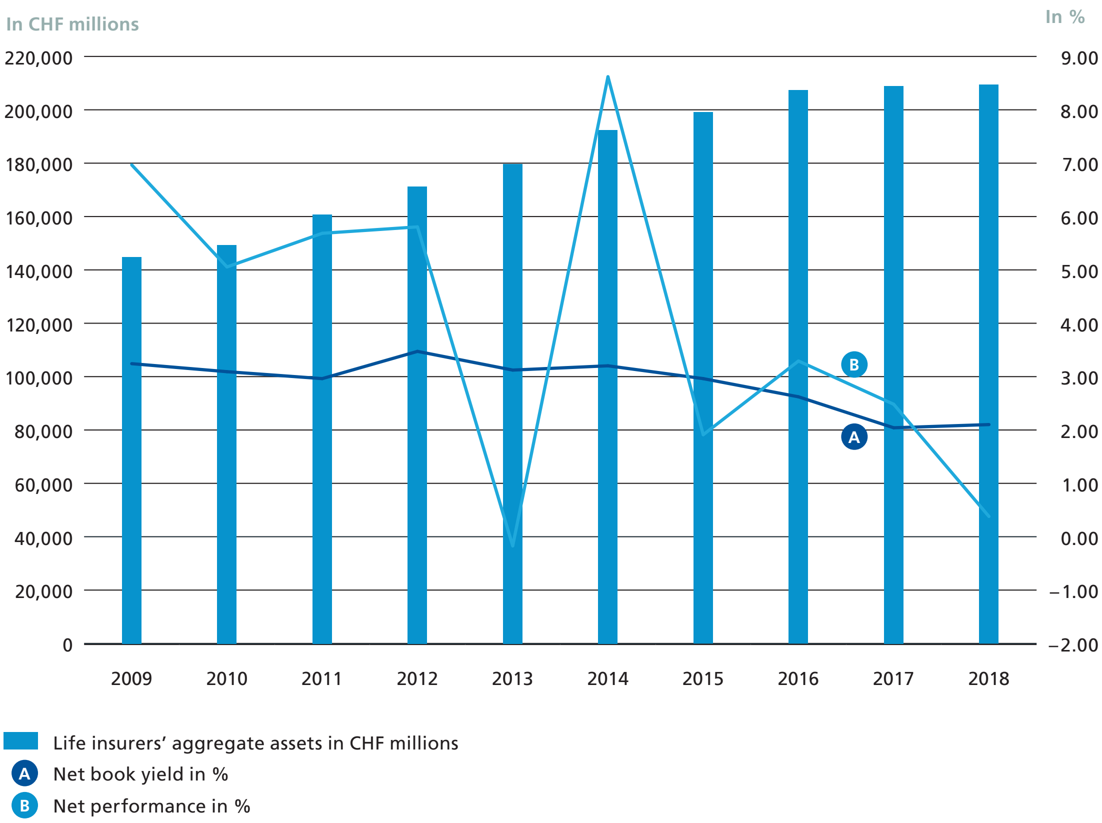
million) in their occupational pension business. The annual result from the occupational pension business is incorporated in the enterprise result; a decision on the appropriation of the result is then made at corporate level.

Savings process burdened by the need to strengthen actuarial reserves for annuities

Life insurers produced positive results in the savings process, with revenues minus expenses yielding CHF 495 million (2017: CHF 670 million). The provisions released in the savings process amounted to CHF 416 million (2017: strengthening of CHF 648), which can be attributed to the previously mentioned one-off effects of AXA's transformation into a risk insurer and the release of provisions for the inflation of risk pensions no longer required.

At 2.10%, the net return on investments (book yield) was slightly higher than in the previous year (2.04%). Between 2009 and 2018, the average return was 2.88% (average from 2008 until 2017: 2.74%). Taking account of the changes in the value of the investments, performance stood at 0.38% (2017: 2.48%).

Aggregate assets, net book yield and net performance of group life insurers, 2009–2018 (Figure 4)



The high proportion of fixed-income securities (liquid assets, bonds and mortgages) – amounting to 74% – is indicative of the types of investment made. Asset management costs (as a percentage of the market value of investments) increased to 28 basis points in the reporting year compared with the previous year's level of 25 basis points.

Risk process: relatively stable results for death and disability risks

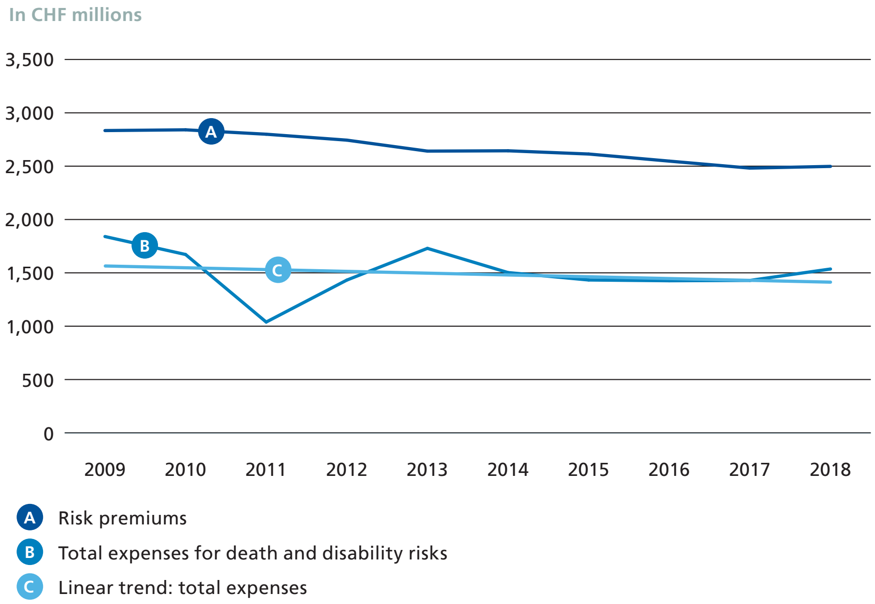
Costs and claims expenditures in the risk process increased by 12% in the reporting year compared with the previous year from CHF 1,454 million to CHF 1,635 million, while risk premiums remained stable. The result (gross) in the risk process fell from CHF 1,009 million to CHF 844 million. As in the previous year, the risk process is therefore the main contributor to the gross result.

Cost process slightly negative

With a deficit of CHF 39 million, the results in the cost process were slightly negative when aggregated across group life insurers. Whereas two years ago the cost deficit was only CHF 3 million, this figure deteriorated further from CHF 19 million in 2017 to CHF 39 million in the reporting year. The reported per capita operating costs rose to CHF 324 (2017: CHF 320).

As management costs for active insured persons, pensioners' collectives and vested benefits policies can be different, FINMA has been requiring operat-

Premiums and total expenses in the risk process, 2009–2018 (Figure 5)



ing costs to be broken down by cost unit since 2012. The per capita figures for 2018 were:

Active insured persons	CHF 415
Pensioners	CHF 440
Vested benefits policies	CHF 73
Total	CHF 377

The difference between the CHF 377 resulting from the income statement and the CHF 324 resulting from the cost process is explained mainly by how claims management costs are recorded; they are included in costs in the income statement but they are recorded in the risk process for the technical breakdown.

Per capita costs differ considerably for each life insurer, with reported management costs per capita varying substantially depending on the life insurer's business model.

The total distribution and acquisition costs of CHF 246 million break down as follows:

Commissions for brokers and agents:	CHF 107 million
Commissions for own sales force:	CHF 95 million
Other acquisition costs:	CHF 44 million

The breakdown of distribution costs – data which FINMA has been collecting since 2013 – has shown that group life insurers generally use internal and external distribution channels, although to greatly varying degrees. On average, group life insurers spend 28% of their costs on distribution, marketing and advertising and 72% on general administration and claims management, as shown in Figure 6.

Distribution costs per active insured person came to CHF 132 (2017: CHF 124). They accounted for around 1% of the gross premium volume generated in 2018.

Technical provisions: significance and function

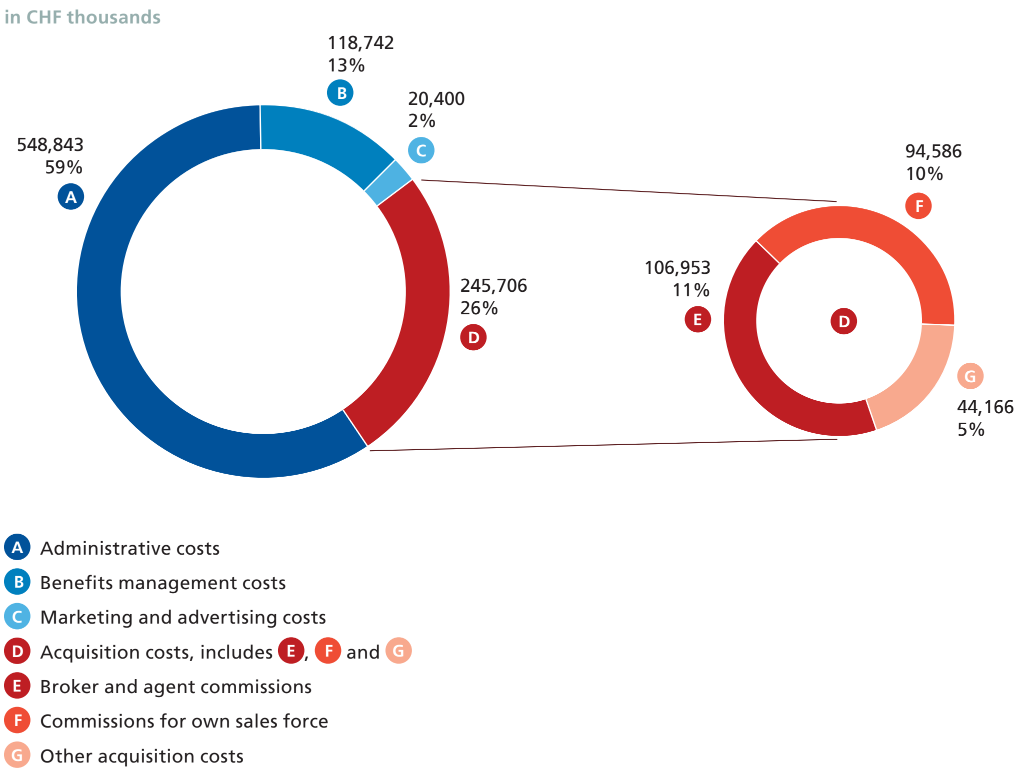
All life insurers must ensure that their technical provisions are sufficient to meet their commitments (Art. 16 ISA). Technical provisions consist of retirement savings, actuarial reserves for current pensions, and further provisions allocated to the insured persons. Insufficient technical provisions must be strengthened so that the obligations from insurance contracts can be met over the long term. This requirement offers the most sustainable protection to insured persons and also builds trust in the Pillar 2 pension system under the Insurance Supervision Act (ISA). One of FINMA's main responsibilities is to ensure that this requirement is met at all times.

Insufficient provisions must be strengthened in line with the approved business plan. Provisions have to be strengthened with the results from the three processes or with the organisation's own assets. Group life insurers must review their technical provisions at least once a year to confirm that they have been correctly calculated in actuarial terms and can sufficiently meet the insurers' contractual obligations sustainably, permanently and securely. Assignments may be made to the surplus fund only once the technical provisions have been adequately covered.

Technical provisions: falling interest rates have necessitated strengthening measures

Actuarial reserves for annuities and other technical provisions (except retirement savings) were valued based on current biometric assumptions and valuation interest rates, which averaged 1.09% at the end of 2018 (2017: 1.31%).

Breakdown of distribution and advisory services costs, 2018 (Figure 6)



Retirement savings fell by CHF 2.4 billion, reaching a year-end total of CHF 98.7 billion. The reduction can be attributed to AXA's withdrawal from the full coverage insurance market: AXA's retirement savings had fallen by around CHF 3 billion as at the end of 2018. A further decline in retirement savings must be expected in the next reporting year as AXA completes its transformation from a full coverage provider to a risk insurer. For group life insurers, the interest rate on mandatory retirement saving was 1.00%, while the average rate for supplementary retirement savings was 0.19% (2017: 0.22%; only guaranteed interest). Participation in the surplus generated must also be included.

Actuarial reserves for current old-age and survivors' pensions have risen further (5%) and now total CHF 40.7 billion. The increase is partially driven by group life insurers' obligation to strengthen their actuarial reserves on account of higher life expectancies and lower interest rates. This affects not only current pension benefits but also losses from future pension conversions because of excessively high conversion rates.

The surplus fund: function and trends

The surplus fund is an actuarial balance sheet item to free up surplus dividends for occupational pension institutions and their insured persons. A total of

CHF 573 million (2017: CHF 539 million), or just over half of the surplus fund at the beginning of the year, was allocated to these occupational pension institutions and their insured persons. This shows that the surpluses generated in one year were passed on rapidly to the insured persons. During the reporting year, a high amount of CHF 1,542 million of the net result was allocated to the surplus fund (2017: CHF 493 million). The high allocation to the surplus fund is due on the one hand to the release of provisions for the inflation of risk pensions no longer required, as previously mentioned, while on the other hand it can be attributed to AXA, which – due to its transformation – released provisions no longer required to the surplus fund.

Transparency facilitates market comparison
Transparency resulting from the disclosure produces a positive effect. Key indicators (e.g. for costs, dividend policy and investments) allow for comparisons, which in turn benefits companies and employees that are looking for pension solutions. However, virtually all group life insurers have cut back on writing new business, and in some cases they are actively reducing their portfolios. Nevertheless, and despite AXA's withdrawal from the full coverage insurance sector, the premium volume remained stable in 2018 at CHF 22.6 billion (2017: CHF 22.4 billion, 2016: CHF 23.3 billion, 2015: CHF 24.8 billion, 2014: CHF 24.7 billion, 2013: CHF 24.3 billion). However, the 2019 reporting year will present a more complete picture in this regard.

Abbreviations

CHF Swiss franc

ISA Swiss Federal Act of 17 December 2004 on the Supervision of Insurance Companies (Insurance Supervision Act; SR 961.01)

ISO Swiss Federal Ordinance of 9 November 2005 on the Supervision of Private Insurance Companies (Insurance Supervision Ordinance; SR 961.011)

OPA Swiss Federal Act of 25 June 1982 on Occupational Old Age, Survivors'0 and Invalidity Pensions

SME Small and medium-sized enterprise

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